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TAGS: EFIN ECON PINR RS
SUBJECT: RUSSIAN STOCK MARKETS CLOSED, TRADING TO RESUME
SEPTEMBER 19

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Classified By: ECON MC Eric T. Schultz, Reasons 1.4 (b/d).

Summary

¶1. (SBU) In an unprecedented development, Russia's leading stock markets remained closed September 18. Limited transactions to close out overnight lending were allowed on the Moscow Interbank Currency Exchange (MICEX) but the exchange was otherwise closed all day, as was the benchmark, dollar-denominated Russian Trading System (RTS). The government has used the suspension to inject still more liquidity into Russia's financial system. However, in a potentially significant step, the government also announced plans to underwrite the rescue of the investment bank at the heart of Tuesday's meltdown. This represents the GOR's most direct intervention to date and is being likened by analysts to the USG-assisted takeover of Bear Stearns by JP Morgan Whether it is enough to restore confidence to the markets, even temporarily, we will see tomorrow, when the markets are set to reopen. End Summary.

Russian Markets Stay Closed

¶2. (SBU) Russian stock markets, in an unprecedented move, remained closed on September 18, with only limited trading allowed on the Moscow Interbank Currency Exchange (MICEX) to allow for the completion of overnight interbank lending transactions, which take place via MICEX. The Federal Financial Markets Service (FFMS), which regulates Russia's

securities markets, issued the suspension order at noon on September 17. The closure order said the markets would remain closed until further notice. Press statements during the course of September 18 from the Finance Ministry noted that both exchanges would be open for the resumption of trading on September 19.

¶3. (SBU) Many in the financial industry were apparently unaware that the markets would remain closed September 18 until that morning, when the markets failed to open. The morning notes from most investment analysts failed to mention the closure, while expressing optimism that the markets would rebound on the strength of an uptick in oil prices.

GOVERNMENT MOVING TOWARD GREATER INTERVENTION

¶4. (C) The exchanges failure to open represents the latest sign of flagging confidence about solvency in the financial and banking sectors. This came despite repeated government efforts to inject liquidity into the system, which have been welcomed by industry analysts. To implement President Medvedev's pledges to support the country's financial sector, the Finance Ministry and Central Bank (CBR) have made more and more funds available to the banking sector. Since late August, the Finance Ministry has increased the frequency and volume of the "loans" (i.e., auctioned-off temporarily available budget funds) it provides and the CBR has increased the scope of its overnight lending. In the last week, the Finance Ministry has placed $6 billion in 5-week loans and $4.7 billion in 1-week loans with the country's largest banks (namely, Sberbank, VTB, and Gazprombank).

¶5. (C) However, according to many analysts disappearing confidence, not a lack of liquidity, is what drove the markets lower and forced the closure. The proximate cause of the market's closure was apparently the news on September 17 that KIT Finance, a brokerage firm that has added a range of financial services to its operations, defaulted on an overnight loan in the interbank lending market. Reports emerged that other banks had defaulted on their overnight obligations, prompting a wave of concerns about which banks were "good" and which were "bad" counterparties. Prices of Sberbank and VTB stock went into meltdown and triggered the trading suspension.

¶6. (SBU) Officials have taken advantage of the suspension in securities trading to try to calm frazzled investor nerves

and reiterate the GOR's readiness to guarantee that needed liquidity is and will be available. On September 18, Finance Minister Kudrin announced that an additional $8 billion in 1-week loans would be auctioned the following day. On September 17, the CBR lowered reserve requirements by 4 percentage points, a change that the Finance Minister claimed would result in roughly $12.0 billion in additional liquidity. The CBR will also augment credit volumes available through its repo lending facility, by providing the face value (as opposed to a discounted value) of the bonds and other debt instruments banks provide as collateral.

¶7. (SBU) Potentially of more significance was President Medvedev's announcement at an economic policy meeting with Finance Minister Kudrin and CBR Chairman Ignatiyev that the GOR was considering using as much as $20 billion to "uphold the stability of the stock market." At the same meeting, Kudrin pledged to make a 3-month deposit of $2.5 billion in budget funds with Sberbank, VTB, and Gazprombank. Kudrin said the funds were to be used to enable another investment bank, Leader Asset Management, which manages Gazprom's pension fund, to acquire KIT Finance. Some analysts have told us they consider the GOR's response to KIT Finance's distress as analogous to the USG-assisted takeover of Bear Stearns by JP Morgan last March.

Comment

¶8. (C) It is hard to predict how the markets will react to the GOR's decision to intervene more directly by supporting KIT Finance's rescue. Many industry insiders have been calling for just such intervention but others have supported Kudrin's cautious approach and have argued that the liquidity injections simply need time to take effect. We may know more tomorrow but this crisis is likely to persist for some time and we will address in more detail septel the evolving tools available to the GOR with which to manage the situation. End Comment.
BEYRLE